

TESTIMONY OF

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ON BEHALF OF

FINANCIAL EXECUTIVES INTERNATIONAL

BEFORE THE

COMMERCIAL ACTIVITIES PANEL

AT A PUBLIC HEARING ON

PUBLIC-PRIVATE COMPETITIONS AND A-76

AUGUST 15, 2001

Members of the Panel. My name is Alan Hungate. I am the Director of Finance for Central Operations for Motorola and Chairman of the Committee on Government Business of Financial Executives International (FEI). Speaking for myself, I have spent approximately 30 years in the field of Government Business working a variety of cost and finance issues including 19 years working at DCAA. It is my pleasure to share FEI's views on the important issues relating to public/private competition.

Financial Executives International (FEI) is a professional organization representing the interests of about 15,000 CFO's, Treasurers, Controllers and other senior financial executives in over 8,000 corporations throughout the United States and Canada, representing both providers and users of financial information. FEI's Committee on Government Business, is authorized to formulate positions and comments on Government policies that impact FEI members doing business with all sectors of the Federal Government.

FEI supports the underlying objectives of the panel to establish more definitive criteria for determining the functions which can be outsourced, standards for comparing costs which reflect sound accountancy, and fair procedures for conducting public-private A-76 competitions. In general, we believe that public-private competitions should employ transparent and neutral procedures, unbiased competitive evaluations, and reflect fundamental fairness concerns. We share the views of others that a reformed A-76 process will increase efficiency, save money, enhance transparency, and improve the quality of services delivered to the public.

Consistent with these broad goals, we make the following recommendations for changes to the public/private competition process:

1. All bias (and the appearance of bias) in the source selection process must be eliminated through greater use of third party evaluators. The government now decides whether to award a contract to a private company or place the work with government employees by using source selection panels comprised of the government employees. This procedure puts private sector competitors at a disadvantage. Source Selection evaluators and decision-makers must have no stake in the outcome of the private/public competition. Additionally, contractors who advise the government on the Most Efficient Organization (MEO) must not be involved in the evaluation of proposals from private industry. This is a fundamental problem.
2. The two-step selection process, which delays the public/private competition until after the private sector bidders have competed against each other, must be eliminated in favor of a single public/private competition. The fact is that the process of public/private competition takes too long, in many cases up to two to four years. Private companies must decide how to spend their bid and proposal money, and will avoid an overly extended and therefore expensive process. The two-step selection process discourages competition to the detriment of the government's ability to obtain

goods and services in the most efficient manner. That process also deters small and medium-sized companies from participating because of lack of resources.

3. The MEO must be evaluated according to the same rules as private industry bidders. The evaluation process is inherently unfair to private companies and favors MEOs for numerous reasons. Accordingly, the following changes must be made:

- a. MEOs must be required to propose on the same basis as private companies. Private companies must propose either fixed-price or cost-reimbursement contracts as the vehicles for performing the work. Both of these vehicles contain limitations on private company payment and cost recovery, which do not apply to the MEOs in a comparable fashion. If an MEO performs the work, the MEO is not subject to funding limitations or other limitation to prevent cost overruns.
- b. The MEO cost estimate is a strawman based on estimates without factual basis. The government must use actual costs like private companies to derive its proposal. These proposed costs include actual wage rate, actual overhead (not the 12 percent factor of assumed overhead), and actual general and administrative expense. Just as private companies are

required to do, MEOs must employ full costing of all indirect activities to the final cost objectives. In this regard, MEOs must adhere to the same cost accounting requirements imposed on private companies for costing and estimating purposes. For example, the government agency competing against private companies must use the same cost accounting rules as private companies for capitalization and depreciation, such as those contained in FAR Part 31 and Cost Accounting Standards (CAS). Another example is the allocation of indirect costs, such as home office and G&A costs, to cost objectives in accordance with CAS.

- c. The 10 percent/\$10 million cost differential threshold for conversion of work to private companies must be eliminated. This threshold obviously favors retaining work within the government and thwarts competition. The playing field should be level.
- d. Most importantly, public/private competitions must be evaluated on the basis of best value, rather than making determinative cost comparisons involving strawmen MEO. We understand the importance of price competition in the overall equation but strongly believe that Best Value criteria embodied in the FAR should apply in the final competitive

evaluation of the public and private sector competitors.

Factors such as problem solving approaches, management team and key personnel, past performance, special scientific and technical qualifications, and workforce flexibility are all important factors which must be considered in addition to cost.

4. The MEO must be held accountable in performance according to the same rules as private companies. The fact is that work performed by government employees after a public/private competition is not subject to the same accountability as a contract placed with a private company. The same accountability rules must apply to the public sector as apply to the private sector.
 - a. The government agency selected to perform work as the result of a public/private competition must be subject to the same “responsibility” determination as a private company. The government agency must be affirmatively determined “responsible” in areas such as: past performance record, financial capability, ability to meet delivery and performance schedule, record of integrity and business ethics, experience, accounting and operational controls, and technical expertise.
 - b. The government agency must keep actual cost records of all direct and indirect costs allocable to the performance of the

work, and such costs must be audited by an independent audit function.

- c. Government agency performance must be documented and maintained in a past performance record for comparison purposes on future public/private competitions.
- d. The government agency must be subject to the same default termination risk as the private sector. This is fundamental: the public sector must face the same risks of failure as a private company.

This committee should give careful consideration to making strong policy recommendations changes which would establish the position, similar to that being asserted by OFPP Administrator Styles, that FAIR Act inventories are a beginning. Recognizing that there continues to be a need to keep inherently governmental functions off the table, there needs to be an acknowledgment (perhaps in modifications to the FAIR Act) that DOD and other government agencies should follow the worldwide industrial trend towards private sector outsourcing in the following “best candidate” areas: payroll, benefits management, real estate management, claims administration, human resources, internal audit, sourcing/procurement, finance and accounting. These trends documented in the Price Waterhouse Coopers’ global decision-maker’s study on business process outsourcing, were matched by positive feedback:

84% of the business executives surveyed expressed overall satisfaction with the results of outsourcing.

66% of those surveyed felt that shareholder's equity was enhanced; and

67% felt that outsourcing improved their company's competitive position.

As this pertains to the issues under discussion by the A-76 panel, there should be an effort to establish a clear standard where outsourcing and/or privatization (not public private competitions) is the outcome unless there is insufficient diversity in the private sector to deliver qualified bidders. We understand that this will cause some personnel displacement and in that context, the issues pertaining to contracting schemes and costs do not fully address the very important issue of ensuring a soft-landing for federal workers who are displaced as a result of public-private competitions and incentivizing private sector bidders to retain qualified workers from the public sector. A positive step could be to transition a winning public sector bidder to a privatized operation using an ESOP buy-in process for the former public sector employees. We ultimately, ultimately, should not lose sight of the objective to ensure that outsourcing decisions should be made on the basis of sound cost analysis and other factors which allow us to make informed business decisions. But, in some context the panel needs examine personnel transitional issues to ensure the fair treatment of all affected workers.

We are all interested in maximizing the benefits to be derived from streamlined, truly competitive and balanced A-76 guidelines and implementation. FEI believes that implementing the aforementioned recommendations will be a significant and positive step in that direction.

I would be pleased to answer any question that you might have.